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Before the  
**FEDERAL COMMUNICATIONS COMMISSION**  
*Washington, DC 20554*

**JUN 23 1997**

Federal Communications Commission  
Office of Secretary

In the Matter of )  
 )  
Wireless Telecommunications Bureaus )  
Seeks Comment on Broadband PCS C )  
and F Block Installment Payment Issues )

WT Docket 97-82

**To: The Commission**

**Comments of BIA Capital Corp.**

BIA Capital Corp. ("BIA Capital") hereby submits its comments in the above-referenced proceedings. BIA Capital is an investment banking and financial advisory firm assisting companies in the communications industry to establish strategic, financial, and operating objectives and to arrange equity, mezzanine, and senior debt financing for acquisition and expansion opportunities. BIA Capital is affiliated with the BIA Companies which include BIA Consulting, Inc., a communications industry appraisal firm, and BIA Research, Inc., a publishing and research company focused on the broadcasting and telecommunications industries. The BIA Companies have been actively involved in the PCS industry since its inception. We have prepared a number of studies on PCS industry trends, have developed sophisticated financial models, prepared business plans, and assisted entrepreneurs in their capital raising. As such, we have sufficient grounding for claims and are qualified to make recommendations.

The Commission's ongoing commitment to small business participation in the C Block cannot be met by either a re-auction of the licenses or by prepayment of the government debt.

Our recommendation to the FCC is (i) to modify the C Block payments to an interest free basis, (ii) to subordinate the government's lien position to a limited amount of network-related senior debt, (iii) to clarify its cross-default waiver provisions, and (iv) to ease ownership restrictions. These changes should be sufficient to provide funding to this beleaguered segment of the industry, while meeting the goals of the Federal government. These licensees will represent a far stronger credit risk than they are today, positioned to repay the originally agreed upon amount of the debt. The government debt would also be supported by significant new equity commitments. The FCC would be successful in providing an opportunity for small businesses to be involved in PCS and insuring that this spectrum is activated. Any changes short of this plan are likely only to sustain the constraints on the capital raising efforts of C Block companies.

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## **1. Background to current impediments to raising capital**

Development of the C Block spectrum, particularly for smaller, privately-owned licensees with fewer than 5 million pops, has been stymied despite the efforts of a majority of the C Block PCS operators, their original investors, and the FCC itself. We believe the primary obstacle to more active development of the spectrum has resulted primarily from a confluence of financial issues originating from the government's financing of the cost of C Block licenses. The present structuring of the government installment payment program has created the following impediments to raising capital successfully:

*First, equity investors' return thresholds have increased to mitigate what the investors perceive to be increased risk.*

The attractive government financing term (10 years) and interest rate (7%) led to increased bidding competition in the C Block auction which in turn fueled higher prices. The higher prices, coupled with the proliferation and low prices of spectrum auctioned subsequently have created the perception to investors of increased risk among C Block companies. Additionally, the C Block carriers' delay to market relative to the A and B Blocks has further increased risk.

*Second, the equipment lender (or lessor) has increased its return requirements due to its junior position in the PCS company's capital structure, its heightened selectivity of borrowers (or lessees), and the intense demand for vendor financing.*

The lending (or leasing) terms of equipment manufacturers or related third party financiers have become expensive because of (i) the government's prior lien position, and (ii) the C Block carriers' delays in getting to market and the relative depletion of vendor financing availability which had already been directed to larger A and B Block companies. Most C Block companies are start-ups. The companies will probably not generate positive cash flow for three to four years due to the capital-intensive nature of their businesses. In the absence of hard collateral (on which the government has a prior lien) or sustainable positive cash flow against which it could lend, vendor financing sources have (i) imposed higher interest rates and/or (ii) required credit enhancement in the form of cash reserves or third party guarantees, both of which have increased the cost to the C Block carrier and further squeezed the returns an investor could reasonably expect.

Institutions are under no obligation to invest in or lend to C Block ventures or even PCS at all. If the risk vs. return parameters do not meet their needs, they will simply invest in other industries and in non-US projects, as they are presently doing. The consequence of the investor and lender delay becomes compounded: the longer it takes a C Block competitor to get funded, the more risky that company is perceived to be. A goal for many smaller C Block companies has been to

establish a significant presence in secondary and tertiary markets before their larger A and B Block competitors, who have initially focused on building out major metropolitan markets. Passage of time allows entry by more competitors and permits better establishment of brands by A and B Block carriers and incumbent cellular operators.

## **2. Government's public policy objectives for including entrepreneurial companies in the PCS industry.**

We believe that the government has a genuine and appropriate interest to include small businesses in the PCS industry. We also believe that the public interest is served only if operators build out the spectrum which they have won so that it is not idle for years. It may be noteworthy that many C Block licensees with which we are familiar have niche ideas for services and prices to the public which may not be made available by larger competitors.

How productive is this government initiative to include entrepreneurial companies in the PCS industry if the majority of C Block licensees fail to attract sufficient funding to operate? Additionally, as a senior lender, how protected is the FCC by having a senior creditor position, with a 7% return, in a company which is not yet in operation and has little equity?

## **3. Government options for addressing the current impediments to capital raising efforts**

We believe that the FCC has three options:

- 1) re-auction the spectrum,*
- 2) permit prepayment of the government license debt, at a discount, or*
- 3) revamp the structure of the government financing to existing C Block licensees.*

1) If the FCC re-auctions the C Block spectrum, chances are that new bids will be sharply lower than the existing bids and may come in well below the value of any restructuring, particularly if the recent WCS auctions are any indication. The time (not to mention expense) required to award the spectrum to new bidders would create a substantial delay in getting to market for these new winners, thereby delaying service to the public. In addition, a further delay to market, particularly for secondary markets, will be perceived to further increase the risk to investors which will, therefore, further reduce the new bids. It is not in anyone's best interest to re-auction the spectrum.

2) The FCC could permit licensees to prepay their government obligations today at a discount from the face value of note. Prepayment has the advantage of removing the government and its inherent license lien position from a company's capital structure, and may be feasible for the largest C Block licensees which have access to larger, public pools of capital. However, for smaller, privately-funded companies, the prepayment discount would have to be extreme to offset the sharp increase in capital cost to finance the prepayment. For example, the licensee would be

trading debt capital which costs 7% (government debt) for equity capital which has a cost ranging from 30% to 40%.

It appears unlikely that these smaller companies could raise additional debt in excess of their present network equipment and soft cost needs. Accordingly, funding to buy out the government financing at any price would need to be provided by equity. *The economics of such a prepayment are less, not more, attractive* and would seem to impair further these privately-funded company's ability to raise capital. Therefore, the probable outcome of this strategy will be to **transfer the licenses of smaller C Block companies to larger companies** owned by public or foreign investors.

3) Revamping the terms of the present government financing is believed to be the only course of action which is consistent with the government's stated desire to allow small business to participate in the C Block licensees. The following revisions to the present government financing structure, taken together, are required:

***a) The principal payments from C Block licensees should remain unchanged, but become interest free.***

Too large a disparity exists between C Block prices which averaged \$37.97 per pop and the F Block which averaged \$2.41. Investors which may ultimately be willing to consider an investment in a C Block licensee are typically not candidates for an investment in an A or B Block company. The investment parameters of the C Block are more closely aligned with the F Block, not large, often publicly traded A or B Block companies which have a sharply lower cost of capital. Therefore, it is more important that the C Block price/pop is aligned with F Block pricing.

Our analysis indicates that the present value of the payments of principal and interest of a C Block licensee is 48% of the absolute amount bid (net of the government bidding credit), based on an assumed 20% weighted cost of capital<sup>1</sup>. The present value of an interest free payment stream is 21.4% of the absolute amount, which is comparable to a present value cost per C Block pop of \$8.12. This may still appear high in light of the recent WCS auction bids. However, it is closer to the F Block average price of \$2.41 for one third of the 30 MHz C Block spectrum. A change of this magnitude to the *perceived* cost of the C Block is necessary to attract any meaningful amount of new equity to smaller C Block licensees.

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<sup>1</sup> Our cost of capital calculation for this segment of the C Block assumes the government debt represents 20% of the capital structure at a 7% cost; vendor financing represents 40% at a cost of 12%; equity represents 40% at a 35% cost.

***b) The payments owed the FCC should be subordinate to the payment of senior debt to be raised for network-related equipment and "soft costs".***

A rational capital structure for PCS, as with any capital-intensive industry, requires not only substantial equity investment but also relatively affordable debt to finance equipment acquisition as well as related network "soft costs" which include RF engineering and design, site identification and acquisition, etc. Attracting debt for start-up companies, even if from vendors, is a challenge in itself. However, if this equipment debt is junior in payment to the government entity which regulates the company, ***the increased risk to payment makes this type of capital even more difficult and expensive to obtain.*** This structural impediment eliminates the possibility of attracting third party debt financing unless a credit-worthy third party provides credit enhancement in the form of pledged cash, letters of credit, and/or corporate guarantees. This type of credit enhancement is typically unavailable to all but the largest of the C Block licensees and represents additional cost to the licensee. Alternatively, attempting to fund these equipment and "soft costs" with equity in the absence of debt depresses an investor's returns significantly. Fortunately, some debt sources are believed available to fill this need, given an ability to receive a priority in payment in exchange for their financial commitment.

***c) The FCC should confirm that a default under payments for certain licenses would not cross-default to the licenses of a successful company operated by the same Control Group.***

Cross-default relief is a critical component for both C and F Block licensees. Given the present roadblocks to investors due to the C Block payment structure, it is conceivable that an operator may be successful in attracting funding for its F Block licenses but not its C Block licenses. Both the FCC and the public interest benefits from having healthy F Block companies that are delivering service. However, investors are presently reluctant to commit funds to a F Block company if the FCC could make a claim against it due to a default by a C Block affiliate of the same control group.

***d) The FCC should eliminate any minimum economic ownership level for the Control Group but still retain the voting control requirement for the Control Group.***

Requiring an arbitrary minimum percentage of equity ownership for the Control Group creates an impediment to negotiating an ownership allocation based on the economic benefits each investor/owner is perceived to be offering the C Block company. The FCC should allow competitive market conditions to determine how the value of a C Block company should be allocated among its investors. As long as the voting control resides with the Control Group, the allocation of equity

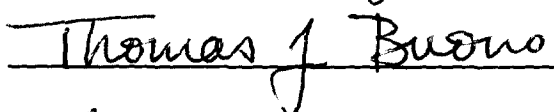
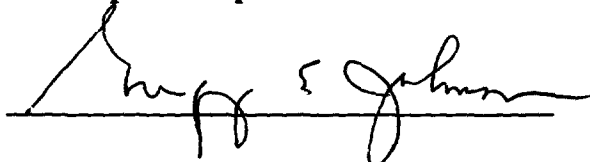
ownership should be based on market forces not by a government regulatory requirement.

***e) The FCC should increase the ownership percentage for individual domestic and foreign institutions to 49.9% from 25% prior to triggering attribution rules, but retain the Control Group's voting control.***

By increasing the ownership percentage that an individual domestic or foreign institution can obtain in a C Block company, the FCC will eliminate complicated financial structures designed to accommodate the differing economic needs of many individual institutions. This increased ownership percentage will (i) offer a meaningful share of ownership to a C Block company's critical strategic partners, and (ii) simplify an entrepreneurial company's ownership structure by reducing the overall number of owners -- without giving up the voting control of the Control Group.

Respectfully submitted,

**BIA Capital Corp.**



By: Gregg E. Johnson  
President

By: Thomas J. Buono  
Executive Vice President

By: Charles A. Wiebe  
Director

14595 Avion Parkway, Suite 500  
Chantilly, Virginia 20151  
(703) 818-8115